Muzakarah
on Failure Resolution of Islamic Financial Institutions

Shariah Discourse 01

Balancing Contractual Sanctity and Systemic Stability: Shariah Insights

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Protecting Your Insurance And Deposits In Malaysia

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Outline

- Research Background
- Research Objectives
- Literature Review
- Application of Shariah Resolution Mechanism within PIDM
- Shariah Principles and Issues in Resolution Mechanism
- Conclusion

Research Background & Objectives

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Background

A global regulatory priority

Post global financial crisis 2008, Recovery and Resolution (RR) frameworks became essential to minimise systemic disruption, protect taxpayers from losses, and maintain critical economic functions.

Unique features of Islamic finance

Riba prohibition, asset-backing and risk-sharing raise unique Sharīʻah and operational issues, requiring tailored approaches.

PIDM's role

As a resolution authority, PIDM is mandated to ensuring that the resolution of Islamic member institutions is compliant with Shariah principles

Research gap

Research and framework on resolution for Islamic financial institutions remain underdeveloped

Research Objectives

1. To analyse debt resolution mechanism from an Islamic perspective.
2. Evaluate the Sharīʻah concepts and principles applicable to resolution mechanisms.
3. Examine the Sharīʻah issues arising from the application of resolution mechanisms.
4. Assess the permissibility of overriding ownership and contractual rights exercised under PIDM's statutory resolution powers.

Islamic Law of Contract

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1 Bilateral in nature

Formed between at least two parties. Abu Zahrah holds that intent expressed by one party alone is a promise (wa'd) or commitment (iltizām), not a contract ('aqd).

2 Grounded in mutual consent

Validity rests on tarādhī (mutual consent). Islam upholds freedom of contract (ḥurriyyah al-ta'āqud); duress or coercion voids the contract.

3 A Sharī'ah-recognised relationship

The relationship between the contracting parties must itself be one that Sharī'ah recognises as legitimate.

4 Immediate effect — with scholarly nuance

Effect begins at the contract session (majlis al-'aqd). Hanafis, Malikis & some Hanbalis allow suspension until a future trigger event; Shāfi'īs & some Hanbalis require immediate effect.

Sanctity of Contracts in Islam

Freedom is recognised, but contractual freedom operates within Shariah

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CORE PRINCIPLE

A valid contract is binding and must be honoured, provided its terms do not contradict Shariah.

1 QUR'AN & SUNNAH

- Qur'an commands believers to "fulfil (all) obligations".
- The Prophetic principle: Muslims must abide by their conditions unless a condition makes the unlawful lawful or the lawful unlawful.

2 FREEDOM + LIMITS

- Autonomy of will is recognised.
- However, parties cannot stipulate terms contrary to Shariah or alter the legal effects prescribed by the Lawgiver.
- A stipulation of riba has no legal effect.
- Thus, contractual freedom is not absolute.

3 SANCTITY + GOOD FAITH

- Contractual obligations should be fulfilled.
- Shariah treats all contracts as contracts in good faith.
- Sanctity serves justice and protects parties from unjust treatment.

In Islam, sanctity of contract is rooted in religion itself — not merely in individual autonomy or economy.

المسلمون على شروطهم إلا شرطاً أحل حراماً أو حرم حلالاً، والشروط الواجب الوفاء بها تكون على الطرفين، وعدم الوفاء بها داخل في إخلاف الوعد الذي هو صفة من صفات المنافقين، وللشروط أحكام بينها أهل العلم – .كتاب شرح *عمدة الأحكام لابن جبرين – ج 48ص 1*

Muslims are bound by their conditions, except for a condition that makes something unlawful lawful or makes something lawful unlawful. The conditions that must be fulfilled are binding on both parties, and failure to fulfil them falls under breaking a promise, which is one of the characteristics of the hypocrites. Conditions have various legal rulings, as explained by the scholars.

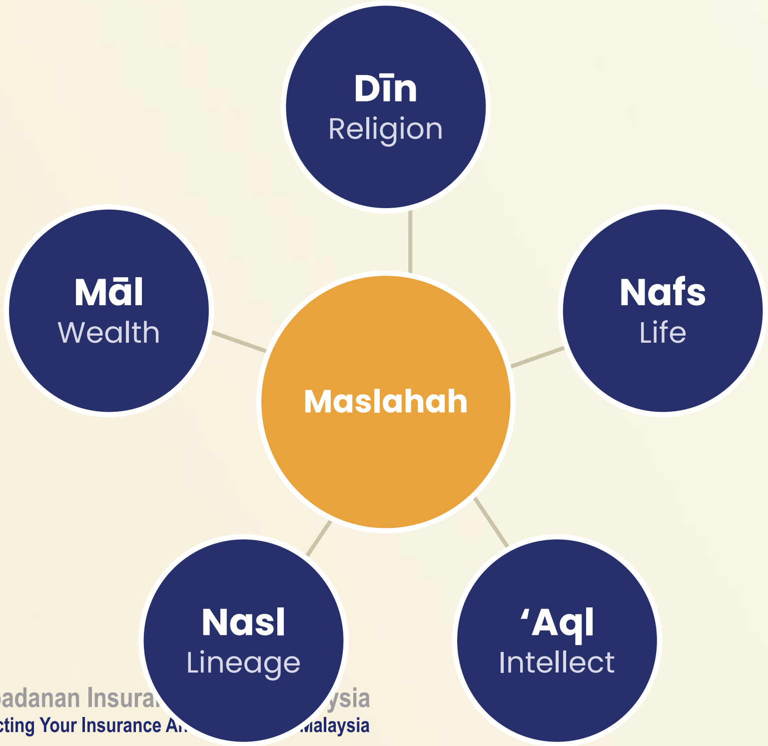
Maqāṣid al-Sharī'ah

IBN 'ĀSHŪR

"The underlying meanings and wisdoms considered by the Lawgiver in legislating rulings — not confined to any specific category of law."

Al-Rasūnī, al-Fāsī, and al-Yūbī converge on the same core idea: safeguarding human welfare (maṣlaḥah) through the Sharī'ah's rulings.

Al-Ghazālī — The Five Essentials (Al-ḥifḍ Al-khams)

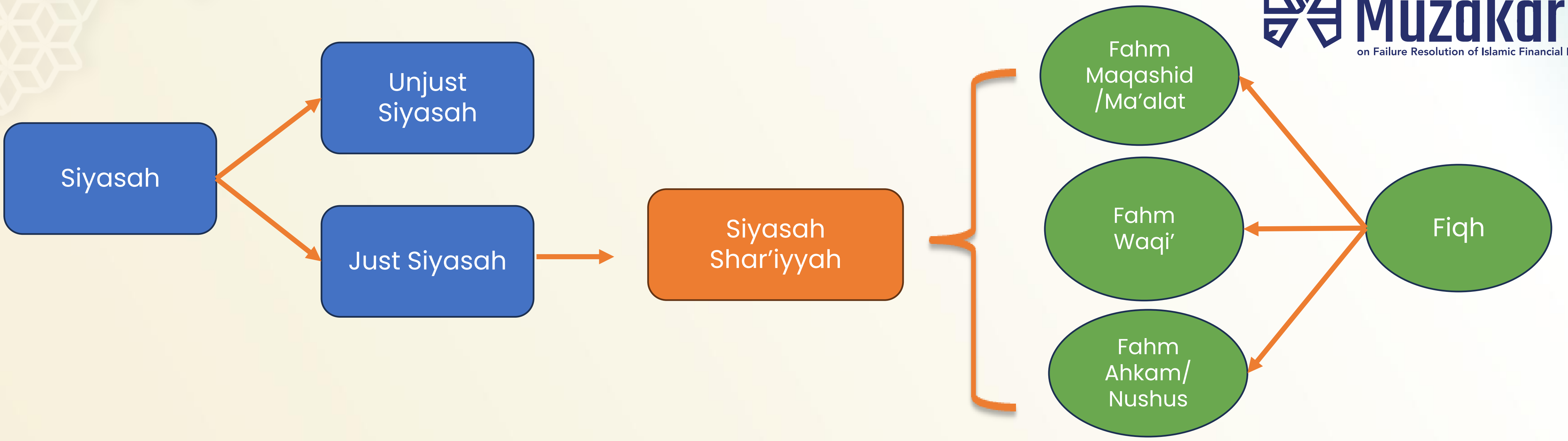


Maṣlaḥah preserves these five — al-Mustaṣfā

Al-Shāṭibī — Three Tiers Of Necessity

Priority runs from the base upward — al-Muwāfaqāt

Siyāsah Shar'iyyah



وَمَنْ لَهُ ذَوْقٌ فِي الشَّرِيعَةِ وَاطِّلَاعٌ عَلَى كَمَالَاتِهَا وَتَضَمُّنِهَا لِغَايَةِ مَصَالِحِ الْعِبَادِ فِي الْمَعَاشِ وَالْمَعَادِ، وَمَجِيئِهَا بِغَايَةِ الْعَدْلِ، الَّذِي يَسَعُ الْخَلَائِقَ، وَأَنَّهُ لَا عَدْلَ فَوْقَ عَدْلِهَا، وَلَا مَصْلَحَةَ فَوْقَ مَا تَضَمَّنَتْهُ مِنْ الْمَصَالِحِ تَبَيَّنَ لَهُ أَنَّ السِّيَاسَةَ الْعَادِلَةَ جُزْءٌ مِنْ أَجْزَائِهَا، وَفَرْعٌ مِنْ فُرُوعِهَا، وَأَنَّ مَنْ لَهُ مَعْرِفَةٌ بِمَقَاصِدِهَا وَوَضْعِهَا وَحَسُنَ فَهْمُهُ فِيهَا لَمْ يَحْتَجْ مَعَهَا إِلَى سِيَاسَةِ غَيْرِهَا أَلْبَتَّةَ.

"

"Whoever possesses a deep insight into the Divine Law (*Sharī ʿah*) and recognizes its perfection—how it completely encompasses the ultimate welfare of people in this life and the Next, and how it delivers the pinnacle of justice for all creation—will realize that **just governance is merely a branch of its branches**."
"Indeed, whoever truly understands the higher aims (*maqāṣid*) and design of the Law will never feel the need for any other form of governance alongside it."

— Ibn al-Qayyim al-Jawziyyah, al-Turuq al-Hukmiyah.

SHARIAH DECISION MAKING FRAMEWORK

فهم المسألة
1 Understand the issue

Understand the issue referred in specific.

فهم الواقع
2 Understand the reality

Understand the reality / practice of contemporary finance.

فهم النصوص
3 Understand Nas Syarak

Understand nas Syarak from the primary and secondary sources by referring to classical and contemporary scholars.

فهم المقاصد
4 Understand Maqasid Shariah

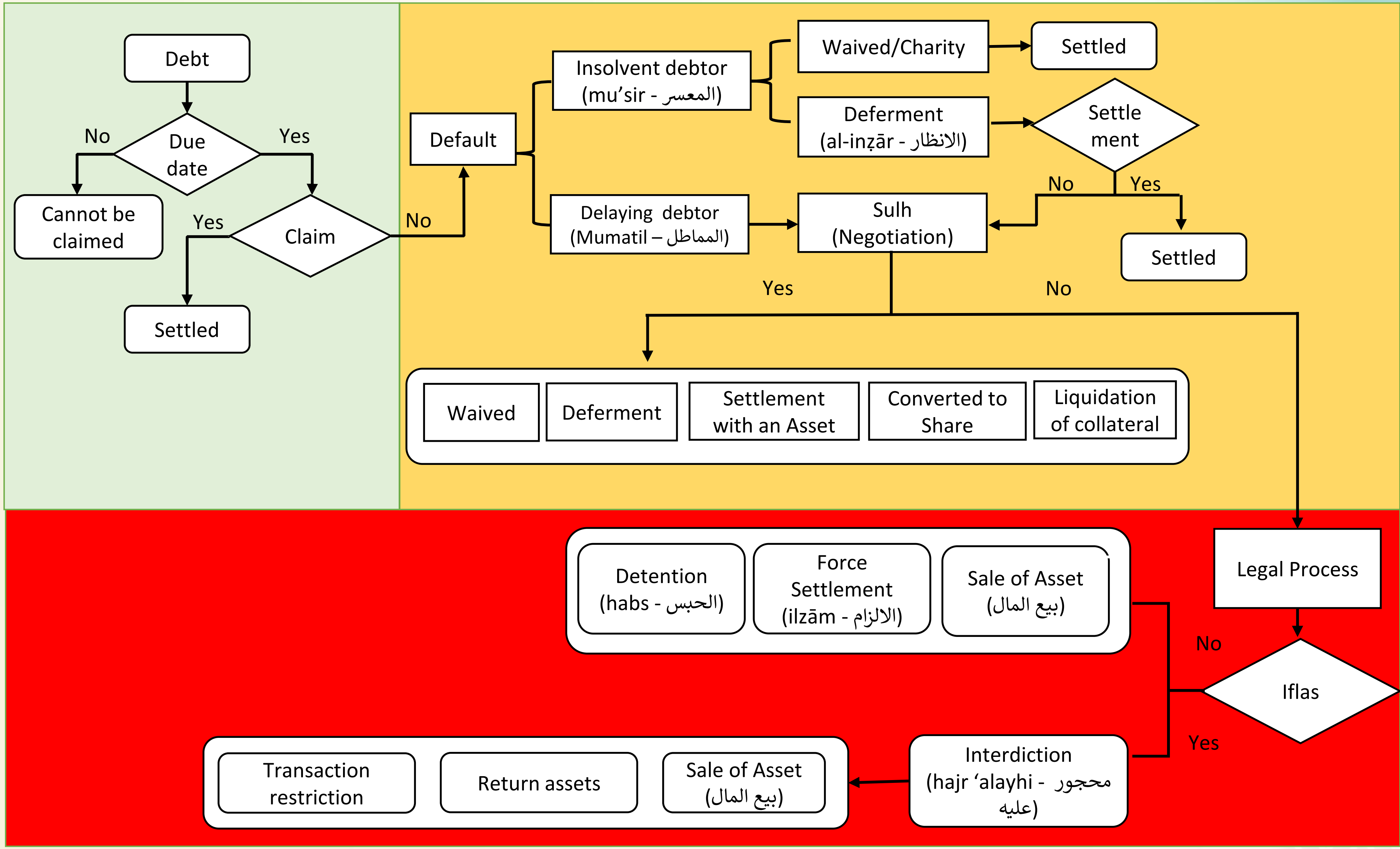
To ensure the recommendation for decision is inline with the maqasid al-Shariah.

فهم الآلات
5 Understand implication

To ensure the decision would give positive impact to the economy, social and environment at large.

Shariah Resolution Framework within PIDM

Debt Resolution Framework in Islam



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Isar (Solvency) إيسار

I'sar (Financial hardship) إعسار

Iflas (Bankruptcy) إفلاس

PIDM Steps in Managing Failing Institutions

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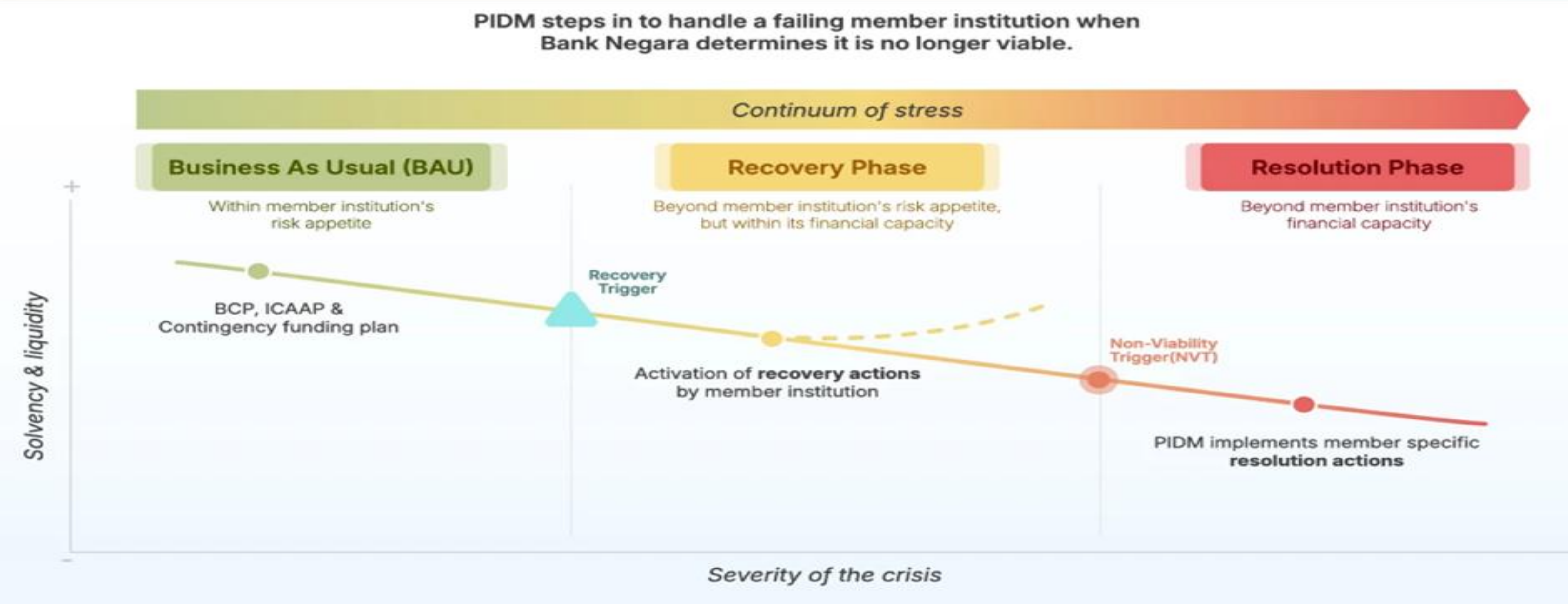


PIDM's Resolution Tools

Muzakarah on Failure Resolution of Islamic Financial Institutions

When Bank Negara Malaysia declares a member institution non-viable, PIDM manages the failure through one of two broad approaches:

Going Concern Resolution

Keep the institution (or parts of it) operating to preserve financial services

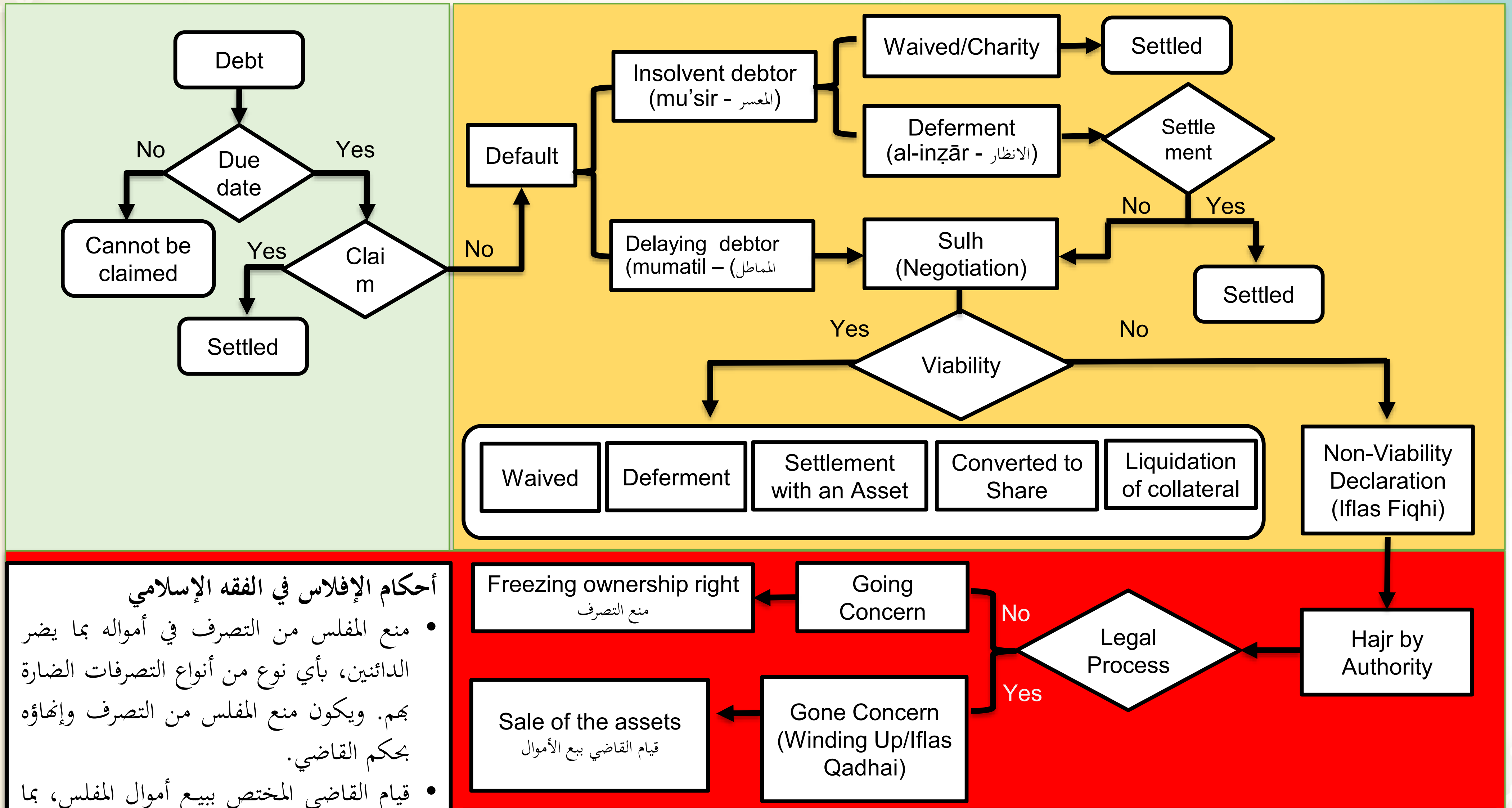
- Transfer to a private sector acquirer (preferred)
- Transfer to a bridge institution
- Partial transfer to an Asset Management Company
- Recapitalisation and restructuring

Gone Concern Resolution

Wind down the institution in an orderly manner

- Court-appointed Liquidator sells remaining assets
- Proceeds distributed by legal order of priority
- Insured deposits reimbursed promptly — no claim needed

Shariah Resolution Framework and its Application within PIDM



أحكام الإفلاس في الفقه الإسلامي

- منع المفلس من التصرف في أمواله بما يضر الدائنين، بأي نوع من أنواع التصرفات الضارة بهم. ويكون منع المفلس من التصرف وإنهاؤه بحكم القاضي.
- قيام القاضي المختص ببيع أموال المفلس، بما هو أصلح وأنفع للدائن والمدين وقسمة ثمنها، وإذا ظهر للمفلس مال جديد جاز للدائنين مطالبته بالوفاء بما هو باق من ديونهم.

مجمع الفقه الاسلامي قرار رقم: 186 (20/1)

وَإِذَا حَجَرَ عَلَيْهِ ثَبَتَ حُكْمَانِ أَحَدُهُمَا: تَعَلُّقُ الدَّيْنِ بِمَالِهِ حَتَّى لَا يُنَفَّذَ تَصَرُّفُهُ فِيهِ بِمَا يَضُرُّ بِالْغُرَمَاءِ، وَلَا تُزَاحِمُهَا الدُّيُونُ الْحَادِثَةُ. وَالثَّانِي: أَنَّ مَنْ وَجَدَ عِنْدَ الْمُفْلِسِ عَيْنَ مَالِهِ، كَانَ أَحَقَّ بِهِ مِنْ غَيْرِهِ –الى ان قال– وَاعْلَمْ أَنَّ التَّعَلُّقَ الْمَانِعَ مِنَ التَّصَرُّفِ، يَفْتَقِرُ إِلَى حَجْرِ الْقَاضِي عَلَيْهِ قَطْعًا وَكَذَا الرُّجُوعُ إِلَى عَيْنِ الْمَبِيعِ.

(روضة الطالبين للنووي)

Business As Usual (Isar/إيسار)

Recovery Phase (I'sar/إعسار)

Resolution Phase (Hajr/qada')

PIDM Perbadanan Insura
Protecting Your Insurance

Overriding Ownership by Authority from Shariah Perspective

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Narrated from Ibn Kaʿb ibn Mālik, from his father, that the Messenger of Allah ﷺ placed a legal restriction on Muʿādh's property and sold it to settle a debt that he owed. Narrated by al-Dāraqutnī, and authenticated by al-Ḥākim.

Commentary on the Hadith

This hadith is evidence that **the ruler or judge may impose a legal restriction (ḥajr) upon a debtor**, preventing him from disposing of his property, and may sell the debtor's property on his behalf in order to settle the claims of his creditors.

— *Subul al-Salām: Commentary on Bulūgh al-Marām*, al-Ṣanʿānī

If a person's assets are **insufficient to cover his debts**, the judge may impose a legal restriction upon him and sell his property on his behalf. This is based on the narration of ʿAbd al-Raḥmān ibn Kaʿb ibn Mālik, who said:

> "Muʿādh ibn Jabal was among the finest young men of his people. He did not retain anything [of his wealth], and he continued to incur debts until his wealth was overwhelmed by debt. The Prophet ﷺ spoke to his creditors on his behalf. If they had been willing to waive anything for the sake of anyone, they would have waived it for Muʿādh because of the Messenger of Allah ﷺ. However, the Messenger of Allah ﷺ sold his property for them, until Muʿādh was left with nothing."

It is also narrated from Kaʿb ibn Mālik that the Messenger of Allah ﷺ placed a legal restriction on Muʿādh and sold his property on his behalf.

— *Al-Muhadhdhab*

وَعَنِ ابْنِ كَعْبِ بْنِ مَالِكٍ، عَنْ أَبِيهِ; أَنَّ رَسُولَ اللَّهِ صلى الله عليه وسلم حَجَرَ عَلَى مُعَاذٍ مَالَهُ، وَبَاعَهُ فِي دَيْنٍ كَانَ عَلَيْهِ. رَوَاهُ الدَّارَقُطْنِيُّ، وَصَحَّحَهُ الْحَاكِمُ.

شرح الحديث: والحديثُ دليلٌ على أن الحاكمَ يحجرُ على المدينِ التصرفَ في مالهِ، ويبيعُه عنهُ لقضاءِ غرمائِه – سبل السلام شرح بلوغ المرام – ت حلاق (الصنعاني)

فإن كان ماله لا يفي بالديون حجر عليه وباع ماله عليه لما روى عبد الرحمن بن كعب بن مالك قال: كان معاذ بن جبل من أفضل شباب قومه ولم يكن يمسك شيئاً فلم يزل يدان حتى أغرق ماله في الدين فكلم النبي صلى الله عليه وسلم غرماءه فلو ترك أحد من أجل أحد لتركوا معاذا من أجل رسول الله صلى الله عليه وسلم فباع لهم رسول الله صلى الله عليه وسلم ماله حتى قام معاذ بغير شيئ وروى كعب بن مالك أن رسول الله صلى الله عليه وسلم حجر على معاذ وباع عليه ماله – المهذب.

REGULATORY	FIQH PERSPECTIVE
BNM's "non-viable" declaration	A judicial ruling (ḥukm qaḍāʾī) that constitutes the legal basis for the process of bankruptcy (iflās) and interdiction/restriction of disposal (ḥajr) — Resolution
BNM	Authority (wilāyah) to impose ḥajr — disposal restriction (منع التصرف)
High Court	Authority (wilāyah) to wind up the company (بيع الأموال)
PIDM	Representative(s) from BNM (Bank Negara Malaysia) and the High Court to undertake ḥajr processes

1 The General Rule

In classical fiqh literature, the imposition of ḥajr by a judge generally requires a petition from the creditors, as ḥajr is instituted primarily to protect their rights and interests.

وَلَا يُحْجَرُ بِغَيْرِ طَلَبٍ فَلَوْ طَلَبَ بَعْضُهُمْ وَدَيْنُهُ قَدْرٌ يُحْجَرُ بِهِ حُجِرَ، وَإِلَّا فَلَا، وَيُحْجَرُ بِطَلَبِ الْمُفْلِسِ فِي الْأَصَحِّ –.منهاج الطالبين

2 The Exception

Where the debt in question constitutes a right of the jihāh ʿāmmah (public interest), the judge may impose ḥajr without waiting for a creditor's petition.

Nihāyah al-Muḥtāj

وَلَا يُحجَرُ عَلَيْهِ) بِغَيْرِ طَلَبٍ (مِنْ غَرَمَائِهِ أَوْ مَنْ هُوَ إِذْ يَخْلُفُهُمْ لِمَصْلَحَتِهِمْ وَهُمْ نَاظِرُونَ لِأَنْفُسِهِمْ، فَإِنْ كَانَ الدَّيْنُ لِمَحْجُورٍ عَلَيْهِ وَلَمْ يَسْأَلْ وَلِيُّهُ وَجَبَ عَلَى الْحَاكِمِ الْحَجْرُ مِنْ غَيْرِ سُؤَالٍ لِأَنَّهُ نَاظِرٌ لِمَصْلَحَتِهِ .وَمِثْلُهُ مَا لَوْ كَانَتْ لِمَسْجِدٍ أَوْ لِجِهَةٍ عَامَّةٍ كَالْفُقَرَاءِ.

Principles of Siyasah Shar'iyyah in Overriding Ownership

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تصرف الإمام على الرعية منوط بالمصلحة

The actions (or policies) of the leader towards the subjects are dependent upon public interest.

المصلحة العامة مقدمة على المصلحة الخاصة

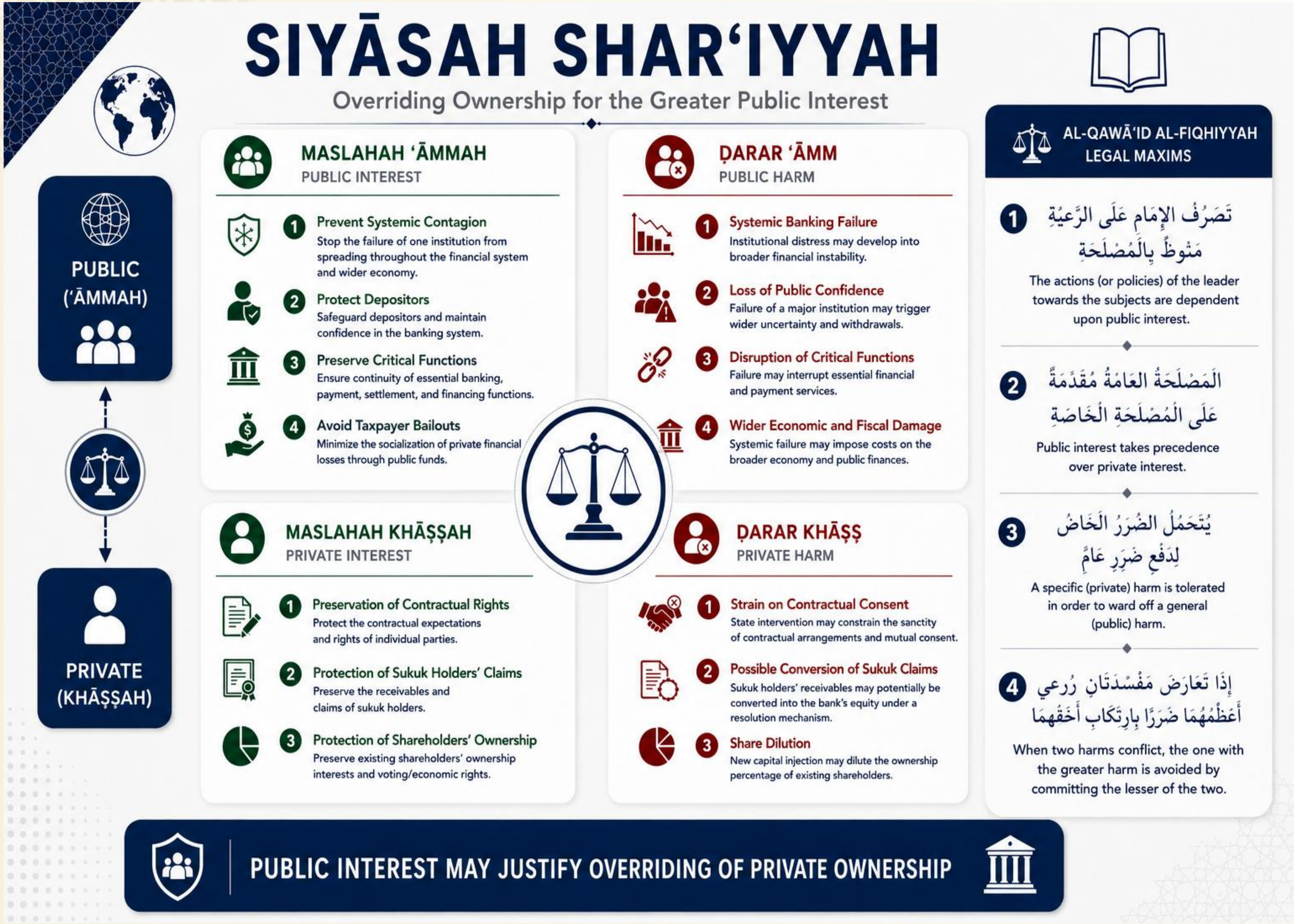
Public interest takes precedence over private interest.

يُتَحَمَّلُ الضَّرَرُ الْخَاصُّ لِدَفْعِ ضَرَرٍ عَامٍّ

A specific (private) harm is tolerated in order to ward off a general (public) harm.

إِذَا تَعَارَضَ مَفْسَدَتَانِ رُوعِيَ أَعْظَمُهُمَا ضَرَرًا بِارْتِكَابِ أَخَفِّهِمَا

When two harms conflict, the one with the greater harm is avoided by committing the lesser of the two.



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Principles of Siyasah Shar'iyyah in Overriding Ownership

Overriding Ownership Framework in the Light of Shariah

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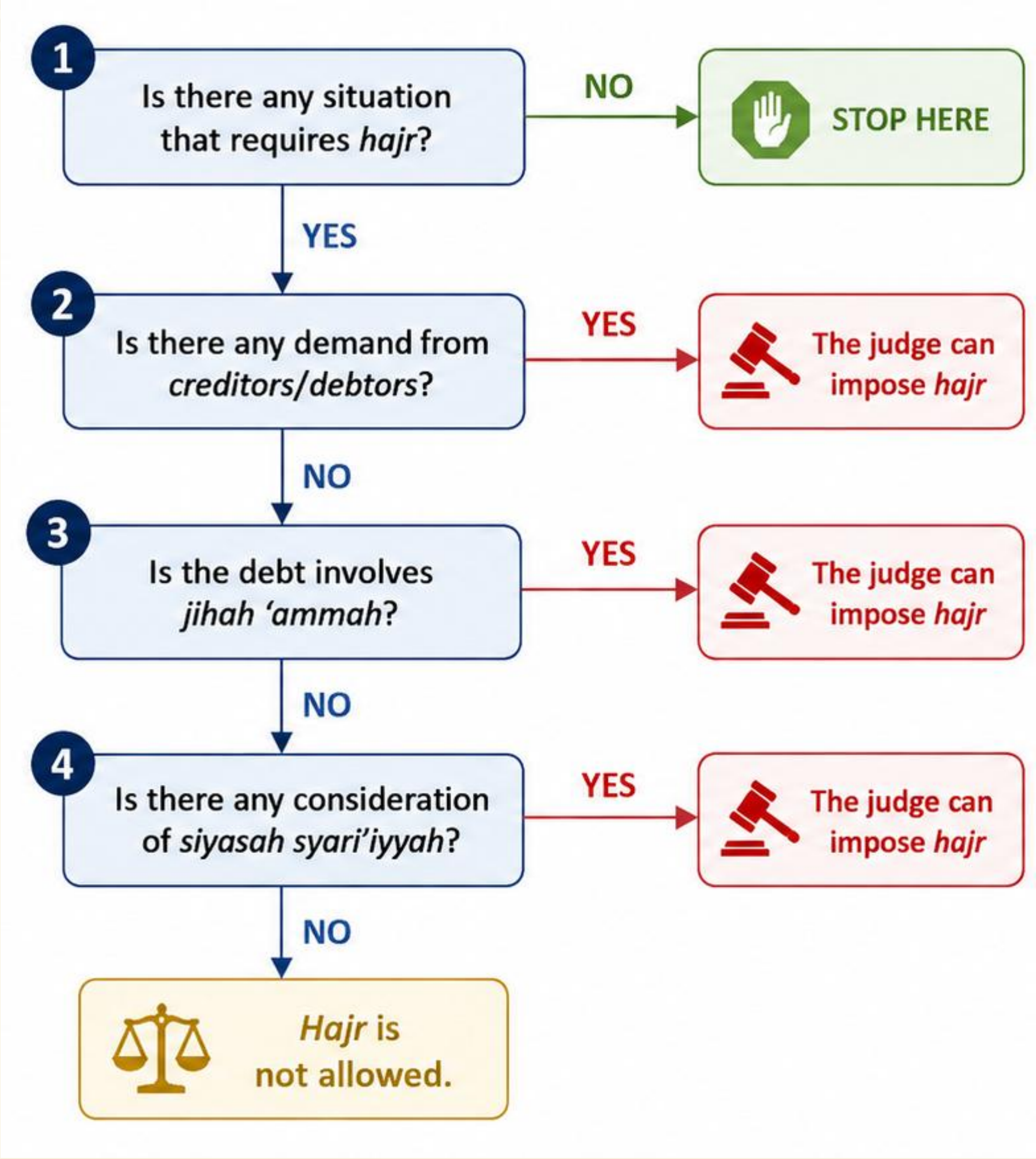

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فَإِنْ كَانَ الدَّيْنُ لِمَحْجُورٍ عَلَيْهِ وَلَمْ يَسْأَلْ وَلِيُّهُ وَجَبَ عَلَى الْحَاكِمِ الْحَجْرُ مِنْ غَيْرِ سُؤَالٍ لِأَنَّهُ نَاظِرٌ لِمَصْلَحَتِهِ ومِثْلُهُ مَا لَوْ كَانَتْ لِمَسْجِدٍ أَوْ لِجِهَةٍ عَامَّةٍ كَالْفُقَرَاءِ

تصرف الإمام على الرعية منوط بالمصلحة

Sharīʻah Concepts and Principles Governing Resolution Mechanisms

Going Concern Scenario

Possible Contracts/Concepts

Transfer* to another company (Private sector acquirer, bridge institution, asset management company)

- Transfer of Asset (financing contracts) → Hawalah Haq, Bay' usul bil Khasmi/Bay' dayn/bay' dayn bi sila', sale of shares (musawamah)
- Transfer of Liability – Islamic Deposits → Hawalah dayn (Qard and Tawarruq), Tanazul haq (Wadiah yad amanah)
- Transfer of Liability /Quasi Equity – Investment Account → Tanazul haq or tandid/fasakh
- Transfer/sale of Shares → Sale of shares (musawamah)

*In the case of a full transfer, the concept of outright sale may be adopted, provided that the tangible assets constitute more than 50% of the debt. If this condition is not met, the concepts of *bay' al-dayn, bay' al-dayn bi al-sila', hawalah, or tawarruq* may be considered.

Recapitalization and Restructuring → Capital Injection

- Injection from Shariah compliant sources
- Injection from Shariah non-compliant sources (in Hajah/darurah situation)

Example of Darurah Condition:
Resolution authority (RA) has exhausted all possible funding options in the resolution actions to avoid systemic risk to the financial industry. However, additional funding is still required, and the only possible solution to address the issue is to obtain funding from an international body – **which can only be offered through a conventional loan arrangement. In this situation, the RA may execute the only possible solution due to the dire necessity of the situation**. (BNM, 2024, hajah and darurah).

Shari'ah Concept Governing Transfer of Asset

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Sales Contract: Murabahah

Loan Contract: Qard Hasan

Non-Performing Financing: Misconduct from PLS and MMQ

Debt-Based Contract

Hawalah Haq/ Bay' dayn/bay' dayn bi sila'/tawarruq

Issue:

- Sale of debt (bay' dayn) at discount

Musharakah Mutanaqisah (MMQ/AITAB)

Leased-Based Contract

Bay' ushul (outright sale)

وَبَيْعُ الْعَيْنِ الْمُسْتَأْجَرَةِ وَهِبَتُهَا وَالْوَصِيَّةُ بِهَا لِغَيْرِ الْمُسْتَأْجِرِ صَحِيحٌ أَيْضًا وَإِنْ لَمْ يَأْذَنْ الْمُسْتَأْجِرُ وَلَا تَنْفَسِخُ) الْإِجَارَةُ – اسنى المطالب.

PLS Contract: Mudarabah/musharakah

Equity-Based Contract

Sale of shares/ownership

Shari'ah Principles Governing the Transfer of Liability: Islamic Deposits

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Wadiah → Trust-Based Contract

Tanazul Haq (right to safeguard)

Issue:

- Consent from depositors

Qard

Tawarruq

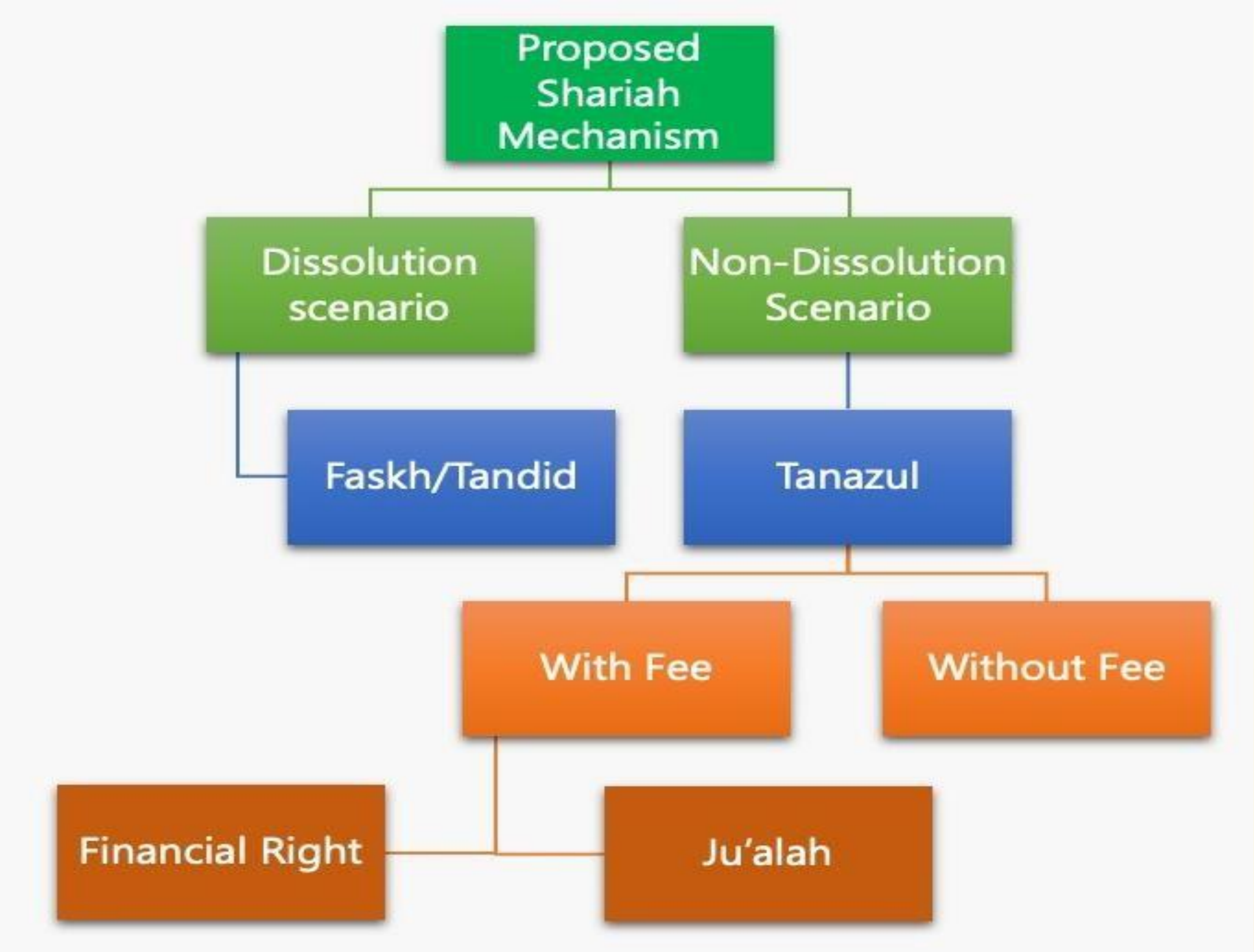
Debt-Based Contract

Hawalah dayn

Issue:

- Creation of new indebtedness to failed bank - Pricing and settlement.
- Hawalah dayn at discount, premium or *bil-ujrah*

Shari'ah Concept Governing Transfer of Islamic Investment Account



Issue:

- Investors' consent
- Tanazul bi 'iwad

Gone Concern Scenario

PIDM Apply to wind up a failing member institution

Court orders winding up

Court appoints a liquidator

Liquidator sells the assets

PIDM pays depositors/takaful participants by priority

Priority of Payments in Winding-Up

Malaysia Deposit Insurance Corporation Act 2011 — ss.134, 134A, 134B

Muzakarah on Failure Resolution of Islamic Financial Institutions

Conventional Member — S.134	Full Islamic Bank — S.134B	Investment Accounts — Carve-out
1 Preferential debts — S.527(1) Companies Act 2016 (eg. Liquidator's cost, Unpaid wages, etc)	1 Preferential debts — S.527(1) Companies Act 2016	1 Outstanding costs/expenses of the investment account
2 Government debts/claims — S.10 Govt. Proceedings Act 1956	2 Government debts/claims — S.10 Govt. Proceedings Act 1956	2 Profit, fees, gains or other remuneration due to the bank
3 **Deposits in Malaysia**	3 **Islamic deposits in Malaysia**	3 Liabilities to investment account holders
4 Other unsecured liabilities	4 Other unsecured Islamic liabilities	*Applies within both S.134A(2)(aa) and S.134B(b) structures*

Islamic Banking Window (S.134A): Two Ring-Fenced Asset Pools

POOL A — Conventional Assets

Applied to liabilities incurred in the course of conventional business, following the S.134 order: preferential debts → Government debts → deposits → other unsecured liabilities.

Surplus flows to the other pool

POOL B — Islamic Banking Assets

RING-FENCED

Not available to meet conventional debts. Applied to Islamic liabilities in priority order: preferential debts → Government debts → Islamic deposits → other unsecured Islamic liabilities.

ss.134(1)(b) & 134A(2)(b), Malaysia Deposit Insurance Corporation Act 2011

Priority of Payment from Shariah Perspective

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Preferential debts	**(قدم على الغرماء مؤنته)** من نفسه وغيره نفقة وكسوة وسكنى، فتعبيري بالمؤنة أعم من تعبيره بالنفقة (في حياته) حتى يقسم ماله لأنه موسر ما لم يزل ملكه هذا –الى ان قال– (و)قدم (مؤنة بيع ماله كأجرة دلال) لأنها من مصالح الحجر - تحفة الطلاب للشيخ زكريا الانصاري
Government Debts	**الْمَصْلَحَةَ الْعَامَّةَ مُقَدَّمَةٌ عَلَى الْمَصْلَحَةِ الْخَاصَّةِ**– الموافقات للشاطبي القاعدة: يُتحمل الضرر الخاص لدفع الضرر العام - القواعد الفقهية وتطبيقاتها في المذاهب الأربعة المؤلف: د. محمد مصطفى الزحيلي
Insured Deposit	Covered by PIDM
Unsecured Liabilities	(و) **قدم (دينه اللازم) له أو ما يؤل إلى اللزوم** (قبل الحجر إن كان به رهن) فيقدم المرتهن بثمنه لتقدم تعلق حقه على حقوق الغرماء (و) قدم (البائع بمبيعه إن لم يقبض ثمنه) من المشتري (ووجده) أي المبيع(بحاله أو ناقصًا نقص صفة) - تحفة الطلاب (القاضي) أي: قاضي بلد المفلس إذ الولاية على ماله ولو بغير بلده له تبعا للمفلس (بعد الحجر) على المفلس (ببيع ماله) بقدر الحاجة (وقسمه) أي: ثمن المبيع الدال عليه ما قبله (بين الغرماء) بنسبة ديونهم — تحفة المحتاج
Investment Account	ذهب الفقهاء إلى أن يد المضارب على رأس مال المضاربة يد أمانة، فلا يضمن المضارب إذا تلف المال أو هلك إلا بالتعدي أو التفريط كالوكيل– الموسوعة الفقهية الكويتية

Conclusion

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Contractual sanctity remains the fundamental principle in Islamic finance, but contractual rights are not absolute where overriding considerations recognised by Sharīʿah arise.

Sharīʿah permits intervention in contractual and ownership rights when necessary to protect legitimate interests, particularly through *ḥajr*, *iflās*, and judicial authority in resolving financial distress.

Maqāṣid al-Sharīʿah and maṣlaḥah provide the overarching rationale for balancing individual contractual rights with the protection of wealth, financial stability, and wider public interest.

Siyāsah Sharʿiyyah supports regulatory intervention where public interest requires it, particularly where a private harm may be tolerated to prevent a greater systemic harm.

PIDM's resolution mechanisms can be accommodated within Sharīʿah, provided that appropriate Shariah concepts, such as *ḥawālah*, *tanāzul*, and other permissible contractual mechanisms, are carefully applied to asset, liability, and investment-account transfers.

A Shariah-compliant resolution framework should therefore balance contractual sanctity, procedural justice, depositor and creditor protection, and systemic stability, with statutory intervention serving as a last-resort mechanism where necessary to safeguard the public interest.

Thank You